

## EUROPEAN HIGH YIELD FUND A-EURO

31 AUGUST 2015

Portfolio manager: Andrei Gorodilov

## Approach and Style

## Performance over month in EUR (%)

Fund	-0.9
Market index	-0.9

BofA ML Global High Yield European Issuers Constrained Index (Level 4 20% Capped)  
Hedged to EUR

Market index is for comparative purposes only.

These figures relate to the fund's past performance, which is not a reliable indicator of future results. The value of investments and any income from them may go down as well as up and an investor may not get back the amount invested. Source of fund performance is Fidelity. Basis: nav-nav with gross income reinvested, in EUR, net of fees.

The fund primarily invests in high yield corporate bonds of European domiciled issuers, diversified across a number of countries and sectors. Emphasis is placed on bottom up name selection, due diligence and ensuring adequate liquidity and diversification due to the asymmetric nature of high yield bond returns. The manager also retains a degree of flexibility to invest in out-of-index strategies as a means of adding performance but adherence to the investment objective remains imperative. The fund is managed according to Fidelity's active philosophy and approach to fixed income investing. This is team-based, but led by the Portfolio Manager to generate attractive risk-adjusted returns through combining multiple, diversified investment positions advised by in-house fundamental credit research, quantitative modelling and specialist traders.

## Market Environment

European high bonds posted negative returns in August of almost 1%. Following a relief rally after the Greek drama dissipated, the asset class suffered from the increased volatility in global markets, uncertainty over the Fed and continued declines in commodity prices and Chinese data. Concerns over the slowdown in the Chinese economy resulted in a deep sell off in commodities and emerging market equities, which fed through into a more broad-based sell-off in risk assets. The People's Bank of China's (PBoC) move to devalue its tightly controlled currency also resulted in an increase in market volatility. Nevertheless, the asset class was still considerably more resilient than a number of other risky assets (such as US high yield) as Eurogroup approved Greece's third bailout and the earning season proved to be largely positive.

## Fund Performance

The fund posted negative returns in August but performed in line with the index. Greek exposure through government bonds and corporates were the largest contributor as the approval of Greece's third bailout by the Eurogroup led to a rally in these bonds. The fund's hedge position through the use of iTraxx credit default swap, protecting against the default of European high yield issuers, also boosted returns as spreads widened amid ructions in Chinese stocks and commodity prices. Against this backdrop, the underweight in banks contributed positively as higher beta sectors sold off alongside risk assets. Likewise, underweight in industrial and energy credits also enhanced returns. Conversely, the overweight in telecommunication sector was the largest detractor with names such as Telemar and Wind holding back returns.

## Fund Positioning

The fund's positioning remains balanced with credit beta (sensitivity to credit spreads) close to the neutral position. At the ratings level, the fund remains underweight BB rated bonds. The fund also retained the overweight in lower-rated credits where the manager has strong conviction. At the sector level, the fund continues to prefer more defensive bonds in communications sector. Tangible asset bases, transparent regulatory environment, stable competitive landscape and prospects of consolidation all contribute to a positive view on this sector. Over the month, the fund increased exposure to IGT given attractive valuations following strong second quarter results. The fund is underweight cyclical corporates such as metals/mining, chemicals, retail and automobiles. Within financials, we have grown less cautious on the sector with regulatory changes forcing stronger balance sheets. Over the month, the fund increased exposure to Royal Bank of Scotland and added a new position in BNP Paribas. Overall, the financials allocation is split between three areas: new alternative Tier 1 debt or contingent convertible bonds, old-style Tier 1 instruments and senior paper from peripheral banks. The fund continues to maintain a healthy liquidity cushion, which provides a buffer during difficult trading conditions and enables quick investments when the market offers attractive opportunities.

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